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In The Know
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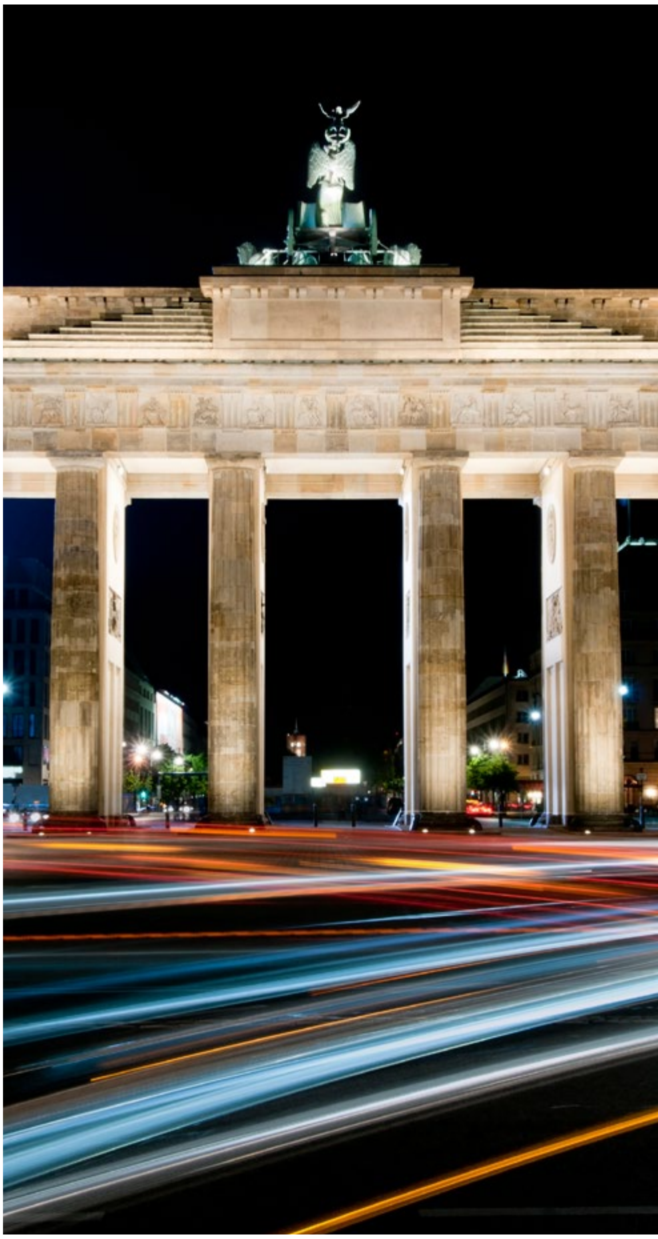
Understanding the Schuldscheindarlehen



Introduction

In recent years, the Schuldscheindarlehen (SSD) has gained considerable traction as a preferred financing instrument among both German entities and international investors. While investors have become more discerning — now subscribing only top-tier creditors — the SSD continues to stand out as an attractive option on the periphery of the debt capital markets, offering appealing economic terms.

This article aims to provide an overview of the SSD, its main characteristics, the corporate acts required, perfection requirements and tax implications.

Main characteristics

An SSD, the English translation of which is promissory loan note, is a bilateral loan agreement governed by German law. It involves transferring a principal amount from the lender to the borrower, which then services the loan by paying a coupon for its duration and repaying the principal amount at maturity. SSDs have become particularly popular as Eurobond market participants seek to diversify their funding sources due to stringent disclosure requirements originally introduced by the Prospectus Directive (now repealed and replaced by the Prospectus Regulation) and the Transparency Directive.

SSDs are mainly denominated in EUR, although trades in other currencies have started to emerge. They are typically unsecured or secured only by corporate guarantees of group members.

The template documentation is negotiated and then used to prepare fixed and floating SSDs, each with different maturities. The maximum term is 10 years, which is the longest term for a loan under German law. Any longer-term funding would require a bond to be issued. Nowadays, SSDs are effectively issued digitally through "Schuldschein issuance platforms". These allow market participants to draft, negotiate and execute the documentation; approach relevant market participants; perform marketing and soundings; carry out the allocation and finally the issuance itself; and handle the SSD over its lifetime from an administrative perspective. The Loan Market Association offers German law template documentation for SSD.

Registered bonds, also known as Namensschuldverschreibungen, are similar to SSDs in many respects. However, they are governed by different regulations and typically have longer durations than SSDs. Registered bonds are securities and can be listed on an exchange or settled via a clearing system like Clearstream or Euroclear. Unlike SSDs, registered bonds may require external ratings and collateral.

For unrated companies or those not yet active in the capital markets, an SSD offers equivalent funding opportunities to private placements conducted under a Euro Medium-Term Note (EMTN) programme but without the need to set up an EMTN platform. SSDs do not directly compete with EMTN issuance due to differences in accounting treatment, making them attractive to investors constrained by the mark-to-market rule.

Funding structure

Typically, a bank in Germany structures and arranges the SSD. Due to banking licensing requirements, the bank collects the funds from investors or lenders, which often do not hold a banking licence. The arranging bank becomes the original lender and then distributes the relevant part of the SSD to the investors. This means that a key requirement for the arranging bank's funding is that it has received all the necessary funds from the investors.

Bilateral in nature

One significant downside of SSDs can be the bilateral nature of each loan agreement. Unlike syndicated loans, where a single agreement governs the relationship between the borrower and multiple lenders, with SSDs each lender enters into a separate bilateral loan agreement with the borrower. This structure can become particularly burdensome during a restructuring process or if refinancing is required in the case of a change of control. Coordinating multiple lenders and obtaining the necessary consent for any amendments or modifications to the loan terms can be time-consuming and complex. Each lender's consent must be obtained individually, which can delay the restructuring or refinancing process and increase administrative burdens.

Default rates

The default rates for SSDs are generally low. According to a report by the Federal Association of German Public Banks (Bundesverband Öffentlicher Banken Deutschlands (VÖB)), the average failure rate of SSDs arranged by VÖB member institutions between 2017 and 2023 was 0.27%. This low default rate corresponds to investment-grade risk, offering investors a high level of security and stability. Further, the legal framework and documentation, typically governed by German law, are concise, robust and tested.

Tax implications

The tax treatment of payments made under an SSD includes analysis of withholding tax, value-added tax, stamp duty and other applicable taxes. As long as the SSD is not profit-linked and the borrower is not a German bank or financial institution, there is no German tax to be withheld by the borrower. Interest income derived from an SSD may be subject to German income taxation if it is attributable to a lender with a German taxable presence. No stamp duty is applicable, and there are currently no documentation taxes for entering into an SSD. Independent tax advice should be sought in connection with any such transaction to ensure the structural integrity of the financing transaction from a tax perspective.

Statistics and market trends

The SSD market has shown resilience in recent years. According to LBBW's market analysis in 2024, the new issuance volume of SSDs reached approximately EUR 20.7 billion, with the number of transactions declining by around 9% compared to the previous year. Despite a challenging economic environment, SSDs continue to attract significant investor interest due to their flexibility and lower administrative burden compared to traditional bonds. Companies from 12 different industries offered a wide range of SSDs to investors in 2024, with non-German companies responsible for approximately 34% of such issuances,. Notable transactions included Rewe Group's EUR 1 billion SSD and Faurecia's EUR 718.9 million SSD.

Conclusion

The SSD offers a flexible and attractive funding option for both German entities and foreign investors. By understanding its main characteristics, corporate acts, perfection requirements, tax implications and market trends, borrowers and lenders can effectively navigate the SSD market and leverage its benefits.

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